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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies.

Rulemaking 06-04-009
(Filed April 13, 2006)

**ADMINISTRATIVE LAW JUDGES' RULING REQUESTING COMMENTS
ON TYPE AND POINT OF REGULATION ISSUES
FOR THE NATURAL GAS SECTOR**

1. Summary

Today's ruling requests comments on the general type and point of regulation to be used to reduce greenhouse gas (GHG) emissions in the natural gas sector. Parties are invited to file comments on the questions contained in this ruling, and any other issues they deem to be related to this topic. Parties may file comments no later than December 12, 2007 and reply comments no later than January 8, 2008.

2. General Instructions

We are requesting comments on the following issues and questions related to regulation of GHG emissions in the natural gas sector. In a July 12, 2007 ruling, we allowed parties to file prehearing conference statements on natural gas issues and comments on preliminary recommendations of the Public Utilities Commission Staff regarding the regulatory treatment of GHG emissions in the natural gas sector (Attachment A to that ruling). Parties should not repeat

comments they submitted in response to the July 12, 2007 ruling. Parties may answer all or any of the following questions. At the end of the questions, parties are asked to submit their comprehensive proposal for how the natural gas sector should be treated for purposes of compliance with Assembly Bill (AB) 32.

Parties should explain their reasons for each answer in detail. Parties are encouraged to refer to their comments filed in response to our November 9, 2007 ruling requesting comments on type and point of regulation issues for the electricity sector, to address the manner in which your recommendations are consistent or differ for the electricity and natural gas sectors.

3. Questions to be Addressed in Comments

3.1. General

- Q1. What do you view as the incremental benefits of a market-based system for GHG compliance in the natural gas sector, in the current California context?
- Q2. Can a market-based system for the natural gas sector provide additional emissions reductions beyond existing policies and/or programs? If so, at what level? How much of such additional emission reductions could be achieved through expansion of existing policies and/or programs?

3.2. Principles or Objectives to be Considered in Evaluating Design Options

In the November 9, 2007 ruling, we described principles or objectives that the Public Utilities Commission Staff proposes be used to evaluate GHG program design options and to develop recommendations regarding a GHG regulatory approach. Recognizing that some of the stated objectives are more applicable to the electricity sector, we repeat the Staff-proposed objectives below (omitting those items that are only relevant to the electricity sector):

- **Goal attainment:** Does the approach being considered have any particular advantages in terms of meeting overall emission reduction goals? For example, does the approach have any advantages to promoting energy efficiency or combined heat and power?
- **Cost minimization:** Is the approach likely to minimize the total cost to end users of achieving a given GHG reduction target?
- **Legal risk:** Is the approach at greater relative risk of being delayed or overturned in court?
- **Environmental Integrity:** Does the approach mitigate or allow the leakage of emissions occurring outside of California as a result of efforts to reduce emissions in California?
- **Expandability:** Would the approach integrate easily into a broader regional or national program? A related consideration is the suitability of the approach as a model for a national or regional program.
- **Accuracy:** Does the approach support accuracy in reporting and, therefore, ensure that reported emission reductions are real?
- **Administrative Simplicity:** Does the approach promote greater simplicity for reporting entities, verifiers, and state agency staff? How easy will the program design be to administer?

Q3. What objectives or principles should the Public Utilities Commission and the Energy Commission use to determine the appropriate method of regulating GHG emissions in the natural gas sector, and why? Please rank the objectives you propose, in order of importance, adding any objectives not covered above.

3.3. Basic Design Questions: Scope of GHG Regulation

For the purposes of answering questions in Sections 3.3, 3.4, 3.5, 3.6, and 3.7, the referenced natural gas sector does not include sources likely to be directly regulated by the California Air Resources Board (ARB), e.g., cement plants, oil refineries, and large point sources, or natural gas used for electricity generation (these emissions are included in the electricity sector).

- Q4. Should GHG emissions from the natural gas sector be capped under AB 32? Are there certain sources of emissions within the sector that should be exempt from an enforceable cap?
- Q5. For each of the following sources of GHG emissions, state whether the sources described should be subject to an enforceable cap and, if so, whether the cap should be covered by a cap-and-trade approach or only by programmatic measures. For sources you recommend covering programmatically, what specific programmatic actions should be taken? For sources you recommend covering in a cap-and-trade program, are there specific programmatic measures that should be undertaken as complementary to the cap-and-trade program? For each source, discuss how your recommended approach is likely to affect rates.
 - a. Natural gas combustion in the residential, commercial, and small industrial segments of the natural gas sector.
 - b. Natural gas combustion by natural gas vehicles.
 - c. Combustion-related emissions from operating the infrastructure (including infrastructure related to proprietary operations) used to deliver natural gas to end users within the State.

- d. Fugitive emissions, including from pipelines, storage facilities, and compressor stations.
- e. Non-combustion uses of natural gas (please specify).
- f. Other sources of natural gas sector emissions not listed above (please specify).

Q6. For the sources you recommend exempting from an enforceable cap, how would emission reductions be achieved?

Q7. As the Public Utilities Commission does not currently have authority to oversee all potential GHG-reducing programs for all kinds of natural gas entities in California, which agency(ies) should regulate in such areas? For example, should ARB require that publicly owned utilities meet energy efficiency targets? Would additional legislation need to be enacted?

3.4. Basic Design Questions: Point of Regulation

Q8. If you believe that the natural gas sector and other sources of emissions related to combustion of natural gas¹ should be included in a cap or cap-and-trade system, where should the compliance obligation be placed: upstream, as close to the fuel source as possible (for example, on natural gas processing plants and pipelines) or midstream/downstream (large point sources and, for smaller users, the local distribution company level)? If you suggest another

¹ Sources include cement plants, oil refineries, large point sources regulated by ARB and natural gas combusted to produce electricity.

option for assigning responsibility, please describe in detail.

- Q9. Should core aggregators or natural gas marketers bear responsibility for the GHG emissions of the customers for whom they procure natural gas?
- Q10. If ARB chooses to individually regulate emissions from facilities in certain sectors as well as emissions from other large point sources, what level of GHG emissions should ARB use as the threshold to define large point sources? Explain your reasoning.

3.5. Deferral of a Market-based Cap-and-Trade System and Coordination with Other States

Section 3.5 of our November 9, 2007 ruling described a scenario in which a California-only cap-and-trade system may not be implemented at this time. Similar questions are asked here for the natural gas sector.

- Q11. In developing recommendation to ARB, should the Public Utilities Commission and the Energy Commission give consideration to actions other states may take regarding the regulation of natural gas sector GHG emissions? If so, how?
- Q12. Is it important that the regulation of California natural gas sector GHG emissions be consistent with actions taken by other states?
- Q13. Would deferral of a cap-and-trade program for the natural gas sector facilitate or hinder California's integration into a subsequent regional or federal program?
- Q14. If neither a regional system nor a national system is implemented within a reasonable timeframe, should California proceed with

implementing its own cap-and-trade system for the natural gas sector? If so, how long should California wait for other systems to develop before acting alone?

- Q15. If a market-based cap-and-trade system is not implemented for the natural gas sector in 2012, how would you recommend addressing early actions that entities may have undertaken in anticipation of a market?

3.6. Relationship to GHG Regulatory Approach in the Electricity Sector

- Q16. For purposes of natural gas GHG regulation under AB 32, does it matter what is decided regarding electricity sector type and point of regulation? For example, would a load-based cap for the electricity sector necessitate a similar type of cap for the natural gas sector, with local distribution companies as the point of regulation? If applicable, explain the relationships you see between the electricity and natural gas sectors for AB 32 purposes.
- Q17. If the electricity sector is not included in a California (or wider) cap-and-trade system, could/should the natural gas sector be included? What are your reasons?
- Q18. What implications might there be for fuel switching if GHG emissions for one sector (electricity or natural gas) are capped and GHG emissions for the other sector are not? Would such fuel switching likely lead to an overall decrease, or increase, in GHG emissions?
- Q19. How should the GHG emissions of cogeneration, combined heat and power, and distributed generation end users be considered and regulated

(e.g., in the electricity sector, in the natural gas sector, or as a point source)?

3.7. Recommendation and Comparison of Alternatives

- Q20. Please explain in detail your proposal for how the natural gas sector should be treated under AB 32. Address whether the following emissions sources should be subject to an enforceable cap, and if so, whether reductions in the cap should be achieved by a cap-and-trade approach or only through programmatic requirements: end-user combustion of natural gas, combustion-related emissions from operating the infrastructure, fugitive emissions from pipelines and compressor stations, and non-combustion uses of natural gas. Identify the appropriate point of regulation for each source of emission that should be included in a cap or a cap-and-trade system. Should there just be a sectoral cap, or entity-specific caps as well? Should there be a cap-and-trade system? Address the relationship between programmatic strategies (e.g., energy efficiency programs and pipeline leak detection programs) and a sectoral cap. Discuss any legal concerns or need for new legislation to implement your recommended approach.
- Q21. Describe how your recommended approach satisfies each one of the principles or objectives set forth in Section 3.2.
- Q22. How does your recommended approach differ from the Public Utilities Commission Staff's preliminary recommendations for the natural gas sector attached to the July 12, 2007 ruling?

4. Filing Requirements

All parties filing comments or reply comments shall file them at the Public Utilities Commission's Docket Office and shall serve them consistent with Rules 1.9 and 1.10 of the Public Utilities Commission Rules of Practice and Procedure and Resolution ALJ-188. The parties shall serve their comments and reply comments on the service list for Rulemaking (R.) 06-04-009 posted at www.cpuc.ca.gov when the filings are made, and shall mail a hard copy of the filings to the assigned Commissioner and assigned Administrative Law Judges.

To support the ability of the Public Utilities Commission and the Energy Commission to develop joint recommendations to ARB, we ask that parties submit their comments and reply comments, both in R.06-04-009 and to the Energy Commission's docket 07-OIIP-01.

Procedures for submitting the filings to the Energy Commission are included here for the parties' convenience. The Energy Commission encourages comments by e-mail attachments. In the subject line or first paragraph of the comments, include **Docket 07-OIIP-01**. When naming your attached file, please include your name or your organization's name. The attachment should be either in Microsoft Word format or provided as a Portable Document File (PDF). Send your comments to docket@energy.state.ca.us and to project manager Karen Griffin at kgriffin@energy.state.ca.us. In addition to electronic filing, **one paper copy** must also be sent to:

California Energy Commission
Docket Office, MS-4
Re: Docket No. 07-OIIP-01
1516 Ninth Street
Sacramento, CA 95814-5512

Therefore, **IT IS RULED** that:

1. As directed in this ruling, parties may file comments on the questions included in this ruling no later than December 12, 2007. Parties may file reply comments no later than January 8, 2008.

2. Parties shall file their comments and reply comments at the Public Utilities Commission's Docket Office and shall serve them consistent with Rules 1.9 and 1.10 and Resolution ALJ-188. The parties shall serve their filings on the service list for R.06-04-009 posted at www.cpuc.ca.gov when the filings are made, and shall mail a hard copy of the comments to the assigned Commissioner and the assigned Administrative Law Judges.

Dated November 28, 2007, at San Francisco, California.

/s/ JOHNATHAN LAKRITZ for
Charlotte F. TerKeurst
Administrative Law Judge

/s/ JOHNATHAN LAKRITZ
Jonathan Lakritz
Administrative Law Judge

INFORMATION REGARDING SERVICE

I have provided notification of filing to the electronic mail addresses on the attached service list.

Upon confirmation of this document's acceptance for filing, I will cause a Notice of Availability of the filed document to be served upon the service list to this proceeding by U.S. mail. The service list I will use to serve the Notice of Availability of the filed document is current as of today's date.

Dated November 28, 2007, at San Francisco, California.

/s/ SANDRA M. JACKSON

Sandra M. Jackson